



DEFENSE CONTRACT AUDIT AGENCY
DEPARTMENT OF DEFENSE
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IN REPLY REFER TO

PAS 730.3a

August 15, 2003
03-PAS-059(R)

MEMORANDUM FOR REGIONAL DIRECTORS, DCAA
ASSISTANT DIRECTOR, OPERATIONS
DIRECTOR, FIELD DETACHMENT, DCAA

SUBJECT: Audit Guidance Changes to the Preaward Survey of Prospective Contractor Accounting System Audits for Major and Nonmajor Contractors and the Post Contract Award Accounting System Audits at Nonmajor Contractors

The changes to the audit programs and audit report shells contained in this memorandum are effective with the receipt of the July 2003 edition of the APPS.

As discussed in MRD 03-PAS-011, *Rescission of MRD 02-PPD-072(R), Audit Guidance on Performing Accounting System Audits at Nonmajor Contractors after Contract Award, dated October 2, 2002*, a Headquarters' Task Force addressed issues that surfaced relating to performing accounting system audits at nonmajor contractors after contract award. In addition, the Task Force evaluated the preaward accounting system survey audit program and audit report. The issues that the Task Force addressed included the appropriateness of the audit steps, the audit report language, the type of opinion to be rendered, and the proper DMIS charging. The Task Force's recommendations were forwarded to the Regions and the Field Detachment for comment. All comments were considered; suggested substantive changes not incorporated were discussed with the suggesting region.

The following changes relate to the audit program for Preaward Survey of Prospective Contractor Accounting System (Enclosure 1).

- The existing program, 17740_AP_NA, Preaward Accounting Survey, Version 3.13, dated April 2003, is being replaced with 17740_AP_Preaward Survey of Prospective Contractor Accounting System Audit. The program was revised and tailored to address the requirements of the SF 1408.
- The preaward survey of prospective contractor accounting system audit is an examination of the accounting system at either major or nonmajor contractors **before** contract award. The chief objectives of this examination are to obtain an understanding of the design of the prospective accounting system to appropriately complete the SF 1408 and to render an opinion on whether the design of the contractor's system is acceptable for award of a prospective Government contract.
- The preaward survey of prospective contractor accounting system audit is initiated upon the request of the contracting officer.

SUBJECT: Audit Guidance Changes to the Preaward Survey of Prospective Contractor Accounting System Audits for Major and Nonmajor Contractors and the Post Contract Award Accounting System Audits at Nonmajor Contractors

- A financial capability audit should not be automatically set up. If the contracting officer requests that the contractor's financial capability be addressed, the assignment should be set up under Code 17600.

The following changes relate to the audit program for Post Contract Award Accounting System Audit at Nonmajor Contractors (Enclosure 2).

- The new audit program is named 17740_AP_Post Contract Award Accounting System Audits at Nonmajor Contractors
- The post contract award accounting system audit is an examination of the accounting system at nonmajor contractors *after* contract award. The major objective of the post contract award accounting system audit is to determine if the contractor's accounting system is adequate for accumulating and billing costs on Government contracts.
- A post contract award accounting system audit is usually performed at the request of the contracting officer when (1) a follow-up audit to a pre-award survey is recommended or (2) a preaward survey was not conducted prior to contract award, and the contracting officer determines that an audit is now required to support contract requirements. Additionally, auditors may self-initiate a post contract award accounting system audit, based on audit risk at a nonmajor contractor location. Generally, once a nonmajor accounting system is determined adequate for accumulating and billing costs on government contracts, future full-scope nonmajor accounting system audits should only be performed when deemed necessary based on audit risk.
- The post contract award accounting system audit program includes comprehensive steps to gain a detailed understanding of the contractor's accounting system (e.g., tracing costs billed to source documentation) sufficient to render an opinion on the adequacy of the system.
- Completion of the audit steps in the program will also assist the auditor in determining if the contractor is eligible to submit interim public vouchers directly to disbursing offices (i.e., direct billing program) (CAM 6-1007.3).
- The procedures in the audit program are not sufficient to render an opinion on the key control activities and objectives that comprise a full-scope audit of internal controls. If the auditor determines that a full audit of the internal control is required, code 11010 should be used for the audit of the billing system internal control and code 11070 should be used for the audit of the accounting system internal control. These and the other ICAPS audits should also be used for all post contract award accounting system audits at major contractors.

The Preaward Survey of Prospective Contractor's Accounting System Audit Report (Enclosure 3) reports on whether the design of the accounting system is acceptable, not acceptable, or acceptable with a recommendation that a follow on accounting system audit be performed after contract award. Highlights of the report changes follow.

SUBJECT: Audit Guidance Changes to the Preaward Survey of Prospective Contractor Accounting System Audits for Major and Nonmajor Contractors and the Post Contract Award Accounting System Audits at Nonmajor Contractors

- The subject of audit was changed to conform to AT 501.70 and emphasize that the purpose is to determine acceptability of the design of the system based on the SF 1408 criteria.
- A directional note was added regarding the subject to require a statement regarding the financial capability audit, if one was requested.
- The inherent limitations statement was moved from the results of audit section to the scope section.
- The procedures previously listed after the identification of the applicable requirements were removed since the procedures are listed on the SF 1408.
- The language in the results of audit was changed to address not only the acceptability of the contractor's accounting system but whether the contractor's system is in operation.

The Post Contract Award Accounting System Audit Report (Enclosure 4) had only minor changes from the report initially issued under MRD 02-PPD-072(R). The activity code changed from 11070 to 17740 since an examination of internal controls is not being performed.

In addition, working paper B was tailored for the preaward survey (Enclosure 5), and working papers B and B-2 were tailored for the post contract award accounting system audit (Enclosure 6). Also, the APPS will have a drop-down box to select either the preaward or the post contract award accounting system audit.

DMIS Enhancements

The DMIS description for activity code 17740 is being revised to include both Preaward Survey of Prospective Contractor Accounting System Audits and Post Contract Award Accounting System Audits at Nonmajor Contractors. As a result, we have modified the processes to set up and disposition Code 17740 assignments in DMIS. For the most part, the DMIS screens will look familiar; however, there are differences which are described in Enclosure 7. All of these changes will be effective with release of DMIS Version 3.1. We expect that that Version 3.1 will be issued at the end of August with each region scheduling deployment.

SUBJECT: Audit Guidance Changes to the Preaward Survey of Prospective Contractor Accounting System Audits for Major and Nonmajor Contractors and the Post Contract Award Accounting System Audits at Nonmajor Contractors

FAO personnel should direct any questions they may have regarding this memorandum to their regional office. Any regional questions regarding policy issues should be directed to Kathryn T. Langley, Program Manager, Auditing Standards Division, at (703) 767-3274. Any regional questions regarding DMIS issues should be addressed to Joyce Friedland, Program Manager, Workload Analysis Division, at (703) 767-2255.

/Signed/
Robert DiMucci
Assistant Director
Policy and Plans

Enclosures: 7

1. Preaward Survey of Prospective Contractor Accounting System Program
2. Post Contract Award Accounting System Audits at Nonmajor Contractors Program
3. Preaward Survey of Prospective Contractor Accounting System Audit Report
4. Post Contract Award Accounting System Audit Report
5. W/P B – Preaward
6. W/P B and B-2 – Post Contract Award
7. Description of DMIS Version 3.1 Modifications

Master Document – Audit Program
Activity Code 17740
Preaward Survey of Prospective Contractor Accounting System
Version 4.0, dated July 2003

B-1	Planning Considerations
Purpose and Scope	
<ul style="list-style-type: none"> The major objectives of this audit are to obtain an understanding of the accounting system to appropriately complete the Preaward Survey of Prospective Contractor Accounting System, SF 1408, and to opine as to whether the design of the contractor's system is acceptable for the award of a prospective Government contract. If requested to perform a Preaward Survey of Prospective Contractor Accounting System Audit on a contractor that has an active government contract, and a recent post contract award accounting system audit has not been performed, contact the requestor to ascertain if a post contract award accounting system audit report would be more useful. If a post contract award accounting system audit has been performed, consider providing a copy of the report to the requestor. Discuss with your supervisor. 	
References	
1. CAM 5-200, "Pre-Award Surveys and Adequacy of Accounting System for Contractual Requirements"	
2. FAR 9-105, "Procedures (for determining contractor qualifications)"	
3. FAR 9.106, DFARS 209-106, "Preaward Surveys"	
4. FAR 52.216-16, "Quarterly Limitation on Payments Statement" (FPI contracts); FAR 52.232-20 and FAR 52.232-21, "Limitation of Cost;" FAR 52.232-22(b), "Limitation of Funds."	
5. CAM 5-202.1, "Preaward Financial Capability Survey"	
6. CAM 14-300, "Contractor Financial Capability Audits and Reporting"	

B-1	Preliminary Steps	WP Reference
1.	Research and Planning	

Master Document – Audit Program
Activity Code 17740
Preaward Survey of Prospective Contractor Accounting System
Version 4.0, dated July 2003

<p>a. Review the audit request to ensure the audit scope addresses any customer concerns. If the contracting officer requests the company's financial capability to be addressed during this audit, set up a separate Code 17600 – Financial Capability assignment to perform a financial capability risk assessment (CAM 14-300). If the audit request does not specifically ask for the financial capability to be audited as part of this audit, contact the contracting officer to determine if he/she wants a financial capability risk assessment performed. Notify the contracting officer of the commencement of the audit and the expected completion date (CAM 4-103).</p>	
<p>b. Obtain information on the proposed government contract (e.g., type and amount of contract, special contract provisions, etc.).</p>	
<p>c. If a previous preaward accounting system survey was completed, summarize any accounting system deficiencies found in the permanent file and the impact of these deficiencies on this audit. If a perm file does not exist or is not current, provide a list of items (e.g., organizational charts, financial statements, policies and procedures, etc.) to be obtained during the field visit to the contractor in advance of the entrance conference, so the contractor has additional time to gather the information. Update the permanent file (See CAM 4-405.1).</p>	
<p>d. If the evidential matter to be obtained during the audit is highly dependent on computerized information systems, document on working paper B (section 5) the type/brand of the accounting software used and your understanding of the design of the system. Determine if the controls are adequately designed to ensure the reliability of the computer based data.</p>	
<p>When sufficient work is not performed to determine reliability (i.e., reduce audit risk to an acceptable level), qualify the audit report in accordance with CAM 10-210.4a.</p>	
<p>e. In planning and performing the examination, consider the fraud risk indicators specific to the audit. The principal sources for the applicable fraud risk indicators are:</p> <ul style="list-style-type: none"> • Handbook on Fraud Indicators for Contract Auditors, Section II. (IGDH 7600.3, APO March 31, 1993) located at www.dodig.osd.mil/PUBS/index.html, and • CAM Figure 4-7-3. <p>Document in working paper B any identified fraud risk indicators and your response/actions to the identified risks (either</p>	

Master Document – Audit Program
Activity Code 17740
Preaward Survey of Prospective Contractor Accounting System
Version 4.0, dated July 2003

individually, or in combination). This should be done at the planning stage of the audit as well as during the audit if risk indicators are disclosed (see CAM 4-702). If no risk indicators are identified, document this in working paper B.	
2. Entrance Conference and Preparation	
Arrange and conduct an entrance conference (see CAM 4-302). Explain to the contractor's representatives that as issues are developed during the audit, they will be furnished to the contractor for fact-finding and timely resolution. This process should facilitate reduced audit cycle time and efforts to respond to and issue the audit report.	
3. Initial Risk Assessment	
Using the information obtained in steps 1 and 2, prepare an initial risk assessment to determine the scope of the examination (W/P B).	

C-1	Preaward Survey (SF 1408)	WP Reference
	Prepare "Preaward Survey of Prospective Contractor Accounting System" (SF 1408) by completing the following audit steps:	
	1. Generally Accepted Accounting Principles. Through observation or discussion, verify that the contractor's accounting system is in accordance with GAAP. Determine if the contractor has or intends to have an accrual basis accounting system. (SF 1408, Section I)	
	2. Proper segregation of costs. Verify that controls exist to preclude direct charging of indirect expense and indirect charging of direct contract costs. (SF 1408, Section II, 2a)	
	3. Direct costs by contract. Verify that the contractor has either a subsidiary job costs ledger or account receivable ledger which accumulates costs by contract at a level of detail consistent with that used by the prospective contractor in its proposal. (SF 1408, Section II, 2b)	

Master Document – Audit Program
Activity Code 17740
Preaward Survey of Prospective Contractor Accounting System
Version 4.0, dated July 2003

4. Allocation of indirect costs. Verify that the indirect costs are accumulated in logical groupings and determine that the groupings are allocated based on benefits accrued to intermediate and final cost objectives. Is the cost accounting system formally documented, with a written description of the contents of bases and pools? (SF 1408, Section II, 2c)	
5. Accumulation of costs under general ledger control. Verify that the contractor's job cost ledger and other books of account are reconcilable and currently posted to the general ledger control accounts. (SF 1408, Section II, 2d)	
6. Timekeeping system. Verify that labor is charged to intermediate and final cost objectives based on a timekeeping document (paper or electronic timecards) completed and certified by the employees and approved by the employees' supervisors. (SF 1408, Section II, 2e)	
7. Labor distribution. Verify that labor cost distribution records are reconcilable to payroll records and that labor distribution records trace to and from the cost accumulation records in labor subsidiary or general ledger accounts. (SF 1408, Section II, 2f)	
8. Interim determination of costs. Determine that the contractor posts contract costs at least monthly to books of account. (SF 1408, Section II, 2g)	
9. Exclusion of Unallowables. Evaluate the contractor's plan to identify and exclude unallowable cost if the contract is awarded. (FAR 31.201-6) (SF 1408, Section II, 2h).	
10. Costs by Contract Line Item: Can the system be expanded to the requisite level of detail, and does the contractor have procedures to determine what this level might be? (SF 1408, Section II, 2i)	
11. Preproduction Costs (Applies primarily to manufacturing contracts): Are these costs routinely segregated to assist in repricing or follow-on contract pricing? (SF 1408, Section II, 2j)	
12. Limitation of Costs: Can the interim indirect expense rates be readily calculated from the books of accounts, and are the interim rates routinely monitored? Who is responsible for monitoring total contract expenditure against contract limitations on price or cost, and how frequently is this reviewed? Are controls in place to ensure compliance with the reporting requirements of FAR 52.216-16 or FAR 52.232-20, -21 and -22? (SF 1408, Section II, 3a)	
13. Billings (e.g. progress payments, public vouchers): Does the	

Master Document – Audit Program
Activity Code 17740
Preaward Survey of Prospective Contractor Accounting System
Version 4.0, dated July 2003

contractor have controls or procedures that would provide that interim billings of direct cost are prepared directly from the books and records, excluding unallowable costs and (except for small businesses) accruals other than payroll? Can billings be reconciled to the cost accounts for both current and cumulative amounts claimed? (CAM 6-1006) (SF 1408, Section II, 3b)	
14. Adequate, Reliable Data: Is the contractor's system capable of producing cost information at a sufficient level of detail for use in pricing follow-on contracts. (SF 1408, Section II, 4)	
Accounting system in operation. Is the accounting system in full operation? If not, which portions are in operation and what is the status of implementing the full accounting system? (SF 1408, Section II, 5)	

D-1	Internal Control Questionnaire (ICQ)	WP Reference
	Prepare or update ICQ, as appropriate, based on the results of this audit. Once complete, file document in Permanent File for future use.	

A-1	Concluding Steps	WP Reference
	1. Summary Steps	
	a. If there are open or partially completed items, follow-up and resolve them at this time and summarize audit results.	
	b. Complete, index and cross reference working papers.	
	c. Discuss results of audit with your supervisory auditor. Hold and document an exit conference.	
	d. Take appropriate action to effect correction of noted deficiencies. This may include additional evaluation under an assignment in another audit area, noncompliance or system deficiency reports, cost suspension or disapproval, etc.	
	e. Prepare draft report and SF 1408 to be furnished as part of the audit report.	
	f. Update the permanent file.	

2. Closing Actions	
Closing actions should be performed in accordance with FAO procedures. These procedures may require either auditors or administrative personnel to perform various closing steps. Completion of these closing actions should be documented (e.g., by initials and date on the CD or working paper folder, etc.) and should include:	
a. Once an audit report is signed, the electronic document should immediately be modified to indicate who signed it, and it should be password protected. The electronic file should then be renamed according to the convention "01 DCAA Report [RORG_ASSIGNMENT NO.] – Final.doc" and changed to a read-only file. Only this file should be stored, transmitted, or otherwise used for official purposes.	
b. Once the report is signed, the signature page of the audit report must be scanned in accordance with Agency standard scanning instructions. For audit packages, the scanned signature page file should be named the same as the audit report (see above) with "-sig" added (i.e., 01 DCAA Report 01101-2002X10100389-Final-sig.tif). There is no requirement to make the file a part of the APPS generated executable file and it may be included separately on the CD containing the APPS generated executable file.	
c. Ensure an electronic copy of the final draft audit report containing the supervisory auditor's initials and date on the top page, cross-referenced to the working papers, is included in the working paper package. The final draft report should include all substantive changes made to the original draft, with cross-referencing updated as necessary. It should differ from the final report only due to minor administrative changes (spelling, format, etc.) made during final processing.	
d. Include an electronic version of the acknowledgement letter in the audit working paper package.	
e. Ensure all working paper files are "read only" and, if necessary, compressed for final storage. Generally, current Agency software should be used to automatically modify all electronic files for storage.	
f. Two complete sets of electronic working papers must be prepared. The "original" set should be stored in the working paper package. The "archive" set is to be stored separately from the working paper package on a single session CD-ROM. If there will be a short-	

Master Document – Audit Program
Activity Code 17740
Preaward Survey of Prospective Contractor Accounting System
Version 4.0, dated July 2003

term need to access the working papers, a third, or "working" set should be stored so as to be available for reference, generally on the LAN. This set should be deleted when no longer needed.	
g. Verify that electronic files stored on removable media are not corrupted and can be unarchived.	
h. Securely enclose the “original” set of electronic files in the working paper package.	

Master Document – Audit Program**Activity Code 17740****Post Contract Award Accounting System Audits At Nonmajor Contractors****Version 2.0, dated July 2003**

B-1	<i>Planning Considerations</i>
<p>To provide general guidance for the audit of the adequacy and suitability of nonmajor contractor accounting systems and practices for accumulating and billing costs under Government contracts. An accounting system is adequate if its procedures are adequate to protect the Government's interest, and is suitable if it is in substantive compliance with CAS (This is true whether or not the contractor is CAS-covered since CAS 401, 402, and 405 are incorporated into FAR). This program is intended to be used for the performance of accounting system audits at nonmajor contractors subsequent to contract award. Accounting system surveys performed at the request of a contracting officer to determine the adequacy of the accounting system for a prospective contract should be performed under Preaward Surveys at Nonmajor Contractors.</p>	
<p>The audit should be directed to determining the adequacy of the accounting system for segregation and billing of costs as required by the contractor's contracts. Update the internal control questionnaire (ICQ) as appropriate. Audits of accounting system internal control for nonmajor contractors are generally not required, unless the risk warrants an audit. The audit steps performed in this audit program are not sufficient to provide a basis to opine on the key control activities and objectives that comprise an audit of internal control, i.e., completion of this program will generally NOT justify a control risk assessment of less than maximum. If the auditor determines that an audit of internal control is required, code 11010 should be used for billing system internal control (audit program APBILL) and 11070 for accounting system internal control (audit program APACTG).</p>	
References	
1. CAM 6-1007.3, "Criteria for Adequate Billing Systems – Nonmajor Contractors"	
2. FAR 31.2, "Contracts with Commercial Organizations"	
3. FAR 52.216-16, "Quarterly Limitation on Payments Statement" (FPI contracts); FAR 52.232-20 and FAR 52.232-21, "Limitation of Cost;" FAR 52.232-22(b), "Limitation of Funds."	
4. CAM 14-300, "Contractor Financial Capability Audits and Reporting"	

B-1	Preliminary Steps	
		<u>WP Reference</u>
1.	Review audit request, if applicable, for matters of particular interest to acquisition officials.	

Master Document – Audit Program

Activity Code 17740

Post Contract Award Accounting System Audits At Nonmajor Contractors

Version 2.0, dated July 2003

2. Review permanent files and consider the impact of the following on the scope of this audit: a. prior accounting system reports/surveys, b. results of other related audits (e.g., proposal audits, financial condition risk assessment/audit, etc.), c. currency of labor (MAAR 6) and material (MAAR 13) audits, d. Internal Control Questionnaire (ICQ) data, (and relevant ICAPS information) if applicable. e. The amount of government contracts by contract type.	
3. If the evidential matter to be obtained during the audit is highly dependent on computerized information systems, document on working paper B-2 the type/brand of the accounting software used and the audit work performed that supports reliance on the computer-based evidential matter. Specifically, document or reference one or more of the following in working paper B-2:	
a. the audit assignment(s) where the reliability of the data was sufficiently established in other DCAA audits.	
b. the procedures/tests that will be performed in this audit to evaluate the accounting system that will also support reliance on the evidential matter, and/or	
c. the tests that will be performed in this audit that will be specifically designed to test the reliability of the computer based data.	
4. Obtain a current organization chart.	
5. Obtain a current Chart of Accounts with descriptions of charges, which can be made to each account (Text of Accounts).	
6. In planning and performing the audit, consider fraud risk indicators specific to the audit being performed. The principal sources for the applicable fraud risk indicators are:	
<ul style="list-style-type: none">• Handbook on Fraud Indicators for Contract Auditors, Section II (IGDH 7600.3, APO March 31, 1993) located at www.dodig.osd.mil/PUBS/index.html.	
<ul style="list-style-type: none">• CAM Figure 4-7-3	
Document in working paper B any identified fraud risk indicators and your response/actions to the identified risks (either individually, or in combination). This should be done at the planning stage of the audit as well as during the audit if risk indicators are disclosed (see CAM	

Master Document – Audit Program**Activity Code 17740****Post Contract Award Accounting System Audits At Nonmajor Contractors****Version 2.0, dated July 2003**

4-702). If no risk indicators are identified, document this in working paper B.	
7. Conduct and document the results of the entrance conference as outlined in CAM 4-302, with particular emphasis on:	
a. Any changes in the accounting system processing job stream since the last audit.	
b. The contractor's monitoring process to ensure that established manual and computerized controls are functioning as intended.	
c. Any identified weaknesses or reported internal control deficiencies and related follow-up actions taken by the contractor.	
8. Using the information obtained in the above steps, prepare an initial risk assessment to determine the scope of the audit (W/P B).	

C-1	Adequacy of Accounting System for Accumulating and Segregating Costs	
		<u>WP Reference</u>
To determine that the contractor's accounting system is adequate for accumulating and segregating costs, use the following steps (expand as necessary depending on the risk assessment).		
1.	Proper segregation of costs. Verify that controls exist to preclude direct charging of indirect expense and indirect charging of direct contract costs.	
2.	Direct costs by contract. Verify that the contractor has either a subsidiary job cost ledger or account receivable ledger which accumulates costs by contract.	
3.	Accumulation of costs under general ledger control. Verify that the contractor's job cost ledger and other books of account are reconcilable and currently posted to the general ledger control accounts.	
4.	Interim determination of costs. Determine that the contractor posts contract costs at least monthly to books of account	
5.	Direct Labor. To the extent possible, the auditor should rely on the results of a MAAR 6 audit in determining the effort needed to be performed under steps (a) through (c) below. If a MAAR 6 audit is scheduled for the current fiscal year, the auditor should consider performing MAAR 6 concurrently with this audit. The auditor should consider performing the following steps in conjunction with	

Master Document – Audit Program

Activity Code 17740

Post Contract Award Accounting System Audits At Nonmajor Contractors

Version 2.0, dated July 2003

audit step D.3. (i.e., tracing costs billed to source documentation).	
a. Document the understanding of the contractor's procedures for accumulating and billing labor costs. This includes the procedures for timekeeping, and processing payroll and labor corrections/transfers.	
b. Timekeeping system. Verify that labor is charged to intermediate and final cost objectives based on timekeeping documents (paper or electronic timecards) completed and certified by employees and approved by employee supervisors.	
c. Labor distribution. Verify that labor cost distribution records are reconcilable to payroll records and that labor distribution records trace to and from the cost accumulation records in labor subsidiary or general ledger accounts.	
6. Direct Material. To the extent possible, the auditor should rely on the results of a MAAR 13 audit in determining the effort needed to be performed under steps (a) through (e) below. If a MAAR 13 audit is scheduled for the current fiscal year, the auditor should consider performing MAAR 13 concurrently with this audit. The auditor should consider performing the following steps in conjunction with audit step D.3. (i.e., tracing costs billed to source documentation).	
(a) Document the understanding of the contractor's procedures for accumulating and billing direct material.	
(b) Verify that direct material is charged to final cost objectives. Trace a sample of direct material charges to supporting documentation (e.g., purchase order, receiving report, invoice, and payment.)	
(c) Verify that direct material is needed for the contract. Trace sampled items to supporting documentation that identifies the contract to which the sampled items will be charged (e.g., bill of material.)	
(d) Evaluate procedures in place for assuring prompt payment to vendors; accounting for discounts taken/lost; and calculating the accounts payable turnover in days (or other procedures which ensure obligations are paid when due).	
(e) Evaluate the procedures on items issued from inventory: (1) Can they be traced to issuance documents? (2) Are they priced in accordance with contractor's disclosed practices?	

Master Document – Audit Program

Activity Code 17740

Post Contract Award Accounting System Audits At Nonmajor Contractors

Version 2.0, dated July 2003

(3) Are they issued for current use rather than for intermediate holding?	
7. Indirect Costs. a. Document the understanding of the contractor's procedures for accumulating and billing indirect costs. b. Verify that indirect costs are accumulated in logical groupings and determine that the groupings are allocated based on benefits accrued to intermediate and final cost objectives. c. Verify that interim indirect expense rates can be readily calculated from the books of accounts, and that the interim rates are routinely monitored. d. Verify that the cost accounting system is formally documented, with a written description of the contents of bases and pools.	
8. Exclusion of unallowables. Verify that the cost ledgers identify expense categories in sufficient detail to isolate unallowable costs. Evaluate the adequacy of the contractor's procedures for identification and exclusion of unallowable cost (FAR 31.201-6). Update Appendix 1 of Internal Control Questionnaire, FAR Cost Principle Assessment.	
9. Costs by contract line item. Verify that the contractor's accounting system accumulates costs at the requisite level of detail, as required by the contract terms and conditions.	
10. Pre-production costs (applies primarily to manufacturing contracts). Verify that these costs are routinely segregated to assist in repricing or follow-on contract pricing.	
11. Verify that the contractor's system produces cost information at a sufficient level of detail for use in pricing follow-on contracts.	
12. Financial Capability. Determine if a financial capability risk assessment or audit has been performed at this contractor in the last year. If so, evaluate the results and assess its potential impact on the contractor's accounting system. If not performed and one is required (CAM 14-300), discuss with the supervisor the option of concurrently performing a financial capability risk assessment with this audit. If the auditor and supervisor decide that a financial condition risk assessment should be performed, set up a separate Code 17600 – Financial Capability.	

D-1	Adequacy of Billing System for Preparing Reimbursement Claims
	<u>WP Reference</u>

Master Document – Audit Program**Activity Code 17740****Post Contract Award Accounting System Audits At Nonmajor Contractors****Version 2.0, dated July 2003**

To determine that the contractor's billing system procedures for preparing cost-reimbursement claims are adequate (CAM 6-1006), use the following steps (expand as necessary depending on the risk assessment).	
1. Limitation of costs. Verify that total contract expenditures against contract limitations on price or cost are monitored and updated on a periodic basis. Verify that controls are in place to ensure compliance with the reporting requirements of FAR 52.216-5, -6, -7, -16, and -17 or FAR 52.232-20, -21 and -22.	
2. Verify that the contractor is up to date on its submission of incurred cost proposals in accordance with contract terms. (FAR 52.216-7(d)(2)).	
3. Verify indirect costs are billed at approved rates (or rates specified in the contract) by evaluating a sample of current invoices (public vouchers and progress payment requests) and evaluating a current contractor billing. (CAM 6-1006) If the contractor does not have indirect billing and/or bidding rates, obtain a submission. If the rates have not been approved (FAR 42.704), evaluate the reasonableness of the submitted rates.	
a. Verify that the rates are acceptable for billing purposes. Reference the working paper package where the rates were evaluated.	
b. Verify that the rates have been adjusted for voluntary deletions and historic unallowable costs.	
c. Verify that the rates are consistent with:	
(1.) The contractor's budgetary data (if supported by cost element detail)	
(2.) The actual rates for the last completed fiscal year	
(3.) The year-to-date experienced rates in the current year	
d. Verify that the contractor adjusts billing rates to reflect actual yearend allowable rates. At the end of the contractor's fiscal year, the contractor should compare the recorded allowable rates to the billing rates to determine if billing rates should be adjusted. If there is a significant difference, billings should be adjusted to reflect either the additional amount due the contractor or credit due the government.	
e. If billing rates are not consistent with c(1)-(3) and d above:	

Master Document – Audit Program

Activity Code 17740

Post Contract Award Accounting System Audits At Nonmajor Contractors

Version 2.0, dated July 2003

(1.)Determine whether the differences can be explained.	
(2.)If the differences are both significant and unexplained, the contractor has a billing system deficiency which should be reported, and the auditor should develop appropriate rates.	
4. Verify/test that interim billings are either prepared directly from the cost accounting records or from other records which are reconciled to the cost accounting records by cost element for all cost-reimbursable work. (For time and material and labor hour contracts, total labor costs billed will not reconcile to the contractor's cost accounting records. Consequently, verify that (a) direct labor hours billed reconcile to the cost accounting records and (b) direct labor has been billed at appropriate contract rates.)	
5. Verify that billings can be reconciled to the cost accounts for both current and cumulative amounts claimed.	
6. Verify that the contractor has procedures to ensure that subcontractor and vendor costs are only included in billings if payment to the subcontractor or vendor will be made in accordance with the terms and condition of the subcontract or invoice and ordinarily within 30 days of the contractor's payment request to the government.	
7. Determine that billings are based on current contract provisions. The total amount billed should not exceed any contract, work order, funding limitation, or any other contract ceiling amount. Identify controls which provide for review of contract billing provisions (see CAM 3-2S1), including but not limited to:	
a. Restriction of billing frequency.	
b. Special withholding provisions.	
c. Contractual unallowable costs.	
8. Verify that the contractor has procedures in place to ensure that interim vouchers include fixed fee and cost withholds in accordance with FAR 52.216-7 and 52.232-7, when appropriate.	
a. Verify that for cost-reimbursement type contracts, if required, the contractor withholds fixed fee after payment of 85 percent of contract fixed fee until a reserve is set aside in accordance with contract terms. The reserve should not exceed 15 percent of the total contract fixed fee or \$100,000 whichever is less. See FAR 52.216-8.	
b. Verify that for time and material and labor hour contracts the contractor withholds 5 percent of billable labor costs, not to exceed a total of \$50,000 per contract. FAR 52.232-7(a)(2).	

Master Document – Audit Program**Activity Code 17740****Post Contract Award Accounting System Audits At Nonmajor Contractors****Version 2.0, dated July 2003**

9. Test the contractor's reconciliation of booked to billed costs. If the contractor's reconciliation schedule shows significant overbilling at either the total or individual contract level, discuss with the supervisor the actions needed to resolve overbilling. If the contractor has been authorized to direct bill, determine whether the contractor should continue to be authorized to direct bill (see CAM 6-1007.3 for Criteria for Adequate Billing Systems – Nonmajor Contractors).	
10. If the contractor is authorized to direct bill, perform the following additional steps, if applicable, to test the contractor's continued eligibility for direct billing as part of this audit. Document in this audit the contractor's continued eligibility for direct billing in accordance with CAM 6-1007.6 Contractor Continued Participation in the Direct Billing Program.	
a. From the sample of vouchers reviewed in step 3, determine that the vouchers are mathematically correct and error free. Verify that all columns have accurate totals showing the computation of the billed quantities and unit prices.	
b. Verify that, when submitting first vouchers directly to the paying office, the contractor provided a copy of the first voucher to the FAO within five days of the submission of the first voucher to the paying office.	
c. If applicable, determine that the contractor is submitting final vouchers within 120 days after settlement of applicable final indirect costs rates as required by FAR 52.216-7(d)(5).	

E-1	Internal Control Questionnaire (ICQ)	
		<u>WP Reference</u>
	Complete/update the Internal Control Questionnaire (ICQ). Based on this update, identify other audit areas requiring evaluation to determine if the contractor's accounting system is adequate for accumulating and segregating costs. Discuss the additional risk areas with the supervisor; add audit steps to address those risk areas, if appropriate.	

A-1	Concluding Steps	
		<u>WP Reference</u>
	1. Discuss results with supervisor.	
	2. Discuss findings and recommended corrective action with contractor	

Master Document – Audit Program

Activity Code 17740

Post Contract Award Accounting System Audits At Nonmajor Contractors

Version 2.0, dated July 2003

representatives. Hold and document the exit conference.	
3. Follow up and resolve open or partially completed items and summarize audit results.	
4. Complete, index, and cross-reference W/Ps.	
5. Take appropriate action to effect correction of noted deficiencies. This may include additional evaluation under an assignment in another audit area, noncompliance or system deficiency reports, cost suspension or disapproval, etc.	
6. If the contractor has EVMS-covered contracts, provide comments in the audit report on whether any findings are likely to impact the contractor's EVMS (10-408.2f). Discuss findings and recommendations relating to the EVMS with the Contract Administration Office EVMS Monitor prior to issuance of the report. Immediately evaluate the impact of these findings on specific EVMS-covered contracts and provide the details in flash EVMS surveillance reports (11-209.2.e).	
7. Update the permanent file.	
8. If unsatisfactory conditions were noted, follow the guidance in CAM 4-800.	
9. Prepare draft report incorporating the contractor's comments and audit rejoinder.	
10. Closing actions should be performed in accordance with FAO procedures. These procedures may require either auditors or administrative personnel to perform various closing steps. Completion of these closing actions should be documented (e.g., by initials and date on the CD or working paper folder, etc.) and should include:	
a. Once an audit report is signed, the electronic document should immediately be modified to indicate who signed it, and it should be password protected. The electronic file should then be renamed according to the convention "01 DCAA Report [RORG-ASSIGNMENT NO.] – Final.doc" and changed to a read-only file. Only this file should be stored, transmitted, or otherwise used for official purposes.	
b. Once the report is signed, the signature page of the audit report must be scanned in accordance with Agency standard scanning instructions. For audit packages, the scanned signature page file should be named the same as the audit report (see above) with "-sig" added (i.e., 01 DCAA Report 01101-2002X10100389 –	

Master Document – Audit Program

Activity Code 17740

Post Contract Award Accounting System Audits At Nonmajor Contractors

Version 2.0, dated July 2003

Final-sig.tif). There is no requirement to make the file a part of the APPS generated executable file and it may be included separately on the CD containing the APPS generated executable file..	
c. Ensure an electronic copy of the final draft audit report containing the supervisory auditor's initials and date on the top page, cross-referenced to the working papers, is included in the working paper package. The final draft report should include all substantive changes made to the original draft, with cross-referencing updated as necessary. It should differ from the final report only due to minor administrative changes (spelling, format, etc.) made during final processing.	
d. Include an electronic version of the acknowledgement letter in the audit working paper package.	
e. Ensure all working paper files are "read only" and, if necessary, compressed for final storage. Generally, current Agency software should be used to automatically modify all electronic files for storage.	
f. Two complete sets of electronic working papers must be prepared. The "original" set should be stored in the working paper package. The "archive" set is to be stored separately from the working paper package on a single session CD-ROM. If there will be a short-term need to access the working papers, a third, or "working" set should be stored so as to be available for reference, generally on the LAN. This set should be deleted when no longer needed.	
g. Verify that electronic files stored on removable media are not corrupted and can be unarchived.	
h. Securely enclose the "original" set of electronic files in the working paper package.	


DEFENSE CONTRACT AUDIT AGENCY
AUDIT REPORT NO. –


[Date]

PREPARED FOR:

ATTN:

,

PREPARED BY:

,

 Telephone No.
 FAX No.
 E-mail Address

SUBJECT: Preaward Survey of Prospective Contractor Accounting System Audit

REFERENCES: *ACO:*
*Relevant Dates: (See Page **Error! Bookmark not defined.**)*
CONTRACTOR:

,

REPORT RELEASE RESTRICTIONS: See Page **Error! Bookmark not defined.**
Page
CONTENTS: Subject of Audit
Executive Summary
 Scope of Audit
 Results of Audit

Audit Report No.

Contractor Organization and Systems
DCAA Personnel and Report Authorization
Audit Report Distribution and Restrictions
Standard Form 1408

SUBJECT OF AUDIT

As you requested on *(date)*, we examined *[insert contractor's name]*'s accounting system to determine whether the design of the system is acceptable for the award of a prospective contract, in accordance with the criteria set forth in FAR 53.209-1(f), Standard form 1408, Preaward Survey of Prospective Contractor Accounting System. By submitting a cost proposal to the Government, *[insert contractor's name]* asserts that its accounting system is acceptable to perform the prospective contract in accordance with the above FAR criteria.

NOTE: *If a financial capability audit was requested, add the following statement: The financial capability audit you requested is (in process or complete) and will be issued in a separate report.*

[Insert contractor's name] is responsible for establishing and maintaining an acceptable accounting system for accumulating costs under prospective Government contracts. Our responsibility is to express an opinion on the acceptability of the design of the accounting system for the award of a prospective contract based on our examination.

EXECUTIVE SUMMARY

If applicable (see 10-210.2), this section gives a brief overview of significant audit findings. Refer to 10-406 for examples. Below is an example of how the section may read when the system is not acceptable for accumulating costs under prospective Government contracts.

The contractor's design of the accounting system is not acceptable for the award of a prospective contract. Our examination disclosed *[insert number of deficiencies]* significant deficiencies in *[insert contractor name]* accounting system that could result in misstated costs. Refer to the Results of Audit section for details of our findings.

SCOPE OF AUDIT

Except for the qualifications discussed below, *[omit if the report is not rendering a qualified opinion and there is no "Qualifications" section within the "Scope" paragraph]*, we conducted our examination in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the examination to obtain reasonable assurance about whether the data and records examined are free of material misstatement. An examination includes:

- obtaining an understanding of internal control for accumulating costs under prospective Government contracts;
- examining, on a test basis, evidence supporting the amounts and disclosures in the data and records evaluated;
- assessing the accounting principles used and significant estimates made by the contractor; and
- evaluating the overall data and records presentation.

We evaluated the accounting system using the applicable requirements contained in:

- Federal Acquisition Regulation (FAR);
- *Defense FAR Supplement (DFARS)*; and
- *Cost Accounting Standards (CAS)* [if applicable].

Our examination was performed from [fieldwork starting date] to [fieldwork completion date].

We believe that our examination provides a reasonable basis for our opinion.

Our examination did not include tests to determine whether internal control is in operation or operating effectively. Our examination was limited to determining whether [insert contractor's name]'s design of the accounting system is acceptable for award of a prospective contract. Accordingly, we express no opinion on the system's operating effectiveness. Because of inherent limitations in any internal control, misstatements due to error or fraud may occur and not be detected. Also, accounting system internal control is subject to the risk that the design of the internal control may become unacceptable because of changes in conditions.

QUALIFICATIONS

Any external factors that restrict or limit the scope of the audit should be clearly described within the scope of audit section under a separate heading entitled "Qualifications" (See 10-407e and 10-210.4). Internal decisions to limit the audit scope are not "qualifications." When necessary to avoid user misunderstanding, scope limitations should be briefly described within the scope of audit section.

RESULTS OF AUDIT

NOTE: *SF 1408, Section II, 5 asks if the accounting system is currently in full operation. Therefore comments on whether the system is (1) in operation, (2) set up, but not yet in operation, (3) anticipated, or (4) nonexistent should be made in the results of audit. Tailor the Results paragraph as appropriate to the individual situation. Generally, the use of comments 2, 3 and 4, would require the use of the second opinion statement which recommends a follow-on audit after contract award.*

In our opinion, [except for the (cite the qualification and the potential impact on the results)] the design of the accounting system is [not], in all material respects, considered acceptable for award of a prospective contract in accordance with the criteria contained in FAR 53.209-1(f). The accounting system is in operation [(or) set up, but not yet in operation (or) anticipated, (or) nonexistent]. As requested, we have completed a Standard Form 1408, *Pre-Award Survey of Prospective Contractor Accounting System* (Attachment, see page x).

NOTE: *If the recommendation on the SF 1408 is “Yes, with a recommendation that a follow on accounting system review be performed after contract award,” use the following opinion statement:*

In our opinion, *[except for the (cite the qualification and the potential impact on the results)]* the design of the accounting system, in all material respects, is considered acceptable for award of a prospective contract in accordance with the criteria contained in FAR 53.209-1(f) with the recommendation that an accounting system audit be performed after contract award. The accounting system is in operation *[(or) set up, but not yet in operation (or) anticipated, (or) nonexistent]*. As requested, we have completed a Standard Form 1408, *Pre-Award Survey of Prospective Contractor Accounting System* (Attachment, see page *x*).

The remaining portion of this section, excluding the last paragraph, should summarize the conditions and recommendations found during the system audit. Refer to 10-408.2 for additional information. Below is an example of how the last paragraph may read when significant deficiencies are found.

Our examination noted certain significant deficiencies in the design of the accounting system. In our judgment, these deficiencies could adversely affect the organization’s ability to record, process, summarize, and report costs in a manner that is consistent with applicable government contract laws and regulations. These conditions are detailed in the “Statement of Condition(s) and Recommendation(s)” on page [xx] and summarized below. Also refer to comments contained in the SF 1408.

[Below is an example of how the paragraph may read when the deficiencies found are not considered significant, but correction would enhance the system.]

During the course of our examination, we also noted other matters involving the accounting system which, although not considered to be significant deficiencies at this time, we believe should be communicated to the management of *[insert contractor’s name]*. These matters are detailed in the “Suggestions to Improve the System” appendix included on page [xx] of this report.

We did not perform a comprehensive examination of the contractor’s overall accounting system and its related internal control. Accordingly, we express no opinion on *[insert contractor’s name]*’s system of internal control taken as a whole.

[Conclude the Results of Audit section of the report narrative with the following additional remarks, as appropriate.]

We discussed the results of our examination with *[Name and Title of contractor representative]* in an exit conference held on *[date]*. *[If there are system deficiencies, summarize the contractor’s reaction here.]* We provided a draft copy of *[the Report]* or *[the Results of Audit]* or *[the Statement of Condition(s) and Recommendation(s)]* and /or *[Other (describe)]* to the contractor’s representative at the exit conference. *[When the contractor provides a formal, written response, it should be referenced within the Results of Audit section and included as an*

Audit Report No.

appendix to the report. Put any rebuttals in the “Auditor’s Response” portion of the explanatory notes and include the following statement.] The complete text of the contractor’s response appears as Appendix [x].

[Use the guidelines provided in 10-210.5e(2) to prepare any other additional remarks.]

STATEMENT OF CONDITION(S) AND RECOMMENDATION(S)

Statements of condition(s) and recommendation(s) are an integral part of the results of audit and should follow the narrative described in the Results of Audit. Alternatively, they may be included in attached appendixes. Refer to 10-409 for detail on the presentation criteria and construction.

CONTRACTOR ORGANIZATION AND SYSTEMS

[This section should furnish pertinent information necessary for the reader to understand the area audited. Refer to 10-410 for additional information. An example of wording for this section for a pre-award accounting system survey follows:]

1. Organization:

[Short name] was incorporated in the state of [name state] on [date]. Sales for fiscal year ended [date] were \$XX million, all sales were to commercial customers. [Short name] has two major operations. Describe organization. [Short name's] sales are about equally divided between the two organizations.

2. Accounting System:

[Short name's] accounting period is from [date] to [date]. [Short name] maintains an accounting system on the [accrual] basis in accordance with generally accepted accounting principles. [Short name's] accounting system is posted on a current basis. Appropriate adjusting entries are made at the end of each month and at year end. [Short name] uses [Name of software] software for its accounting system. [Short name] prepares financial statements on a semiannual and annual basis. The annual financial statements are not audited by external CPAs.

NOTE: *If the contracting officer requests a preaward accounting system survey audit but does not request an audit on the related proposal, contact the CO to ask if information on the contractor's pools and bases would be useful, if yes, include in the report.*

Audit Report No.

DCAA PERSONNEL

Primary contacts regarding this audit:

, Auditor

, Supervisory Auditor

Telephone No. _____

Other contacts regarding this audit report:

, Branch Manager

, Financial Liaison Advisor

FAX No. _____

, Financial Liaison Advisor

E-mail Address _____

General information on audit matters is available at <http://www.dcaa.mil/>.

RELEVANT DATES

[Use this section in demand assignments. These should include, at a minimum, the dates of ACO and PCO requests and the dates of any extensions. The format should facilitate computation of elapsed days (see 10-211 and Fig. 10-2-3).]

AUDIT REPORT AUTHORIZED BY:

[Title]

Audit Report No.

AUDIT REPORT DISTRIBUTION AND RESTRICTIONS

DISTRIBUTION

E-mail Address

ATTN:

,

,
(Copy furnished thru ACO)

ATTN:

Telephone

,

RESTRICTIONS

1. Information contained in this audit report may be proprietary. It is not practical to identify during the conduct of the audit those elements of the data which are proprietary. Make proprietary determinations in the event of an external request for access. Consider the restrictions of 18 U.S.C. 1905 before releasing this information to the public.
2. Under the provisions of Title 32, Code of Federal Regulations, Part 290.7(b), DCAA will refer any Freedom of Information Act request for audit reports received to the cognizant contracting agency for determination as to releasability and a direct response to the requestor.
3. Do not use the information contained in this audit report for purposes other than action on the subject of this audit without first discussing its applicability with the auditor.

Audit Report No.

STANDARD FORM 1408

(Available on FormFlow)



DEFENSE CONTRACT AUDIT AGENCY
AUDIT REPORT NO. XXXX-XXXXX17740XXX



[Date]

PREPARED FOR: Administrative Contracting Officer
ATTN:
[Address]

PREPARED BY: [FAO Name]
[FAO Address]
Telephone No.
FAX No.
E-mail Address *dcaa-faoxxx@dcaa.mil*

SUBJECT: Post Contract Award Accounting System Audit

REFERENCES: ACO: Case No. XXX-XX(XX)-XX

CONTRACTOR: [Contractor Name]
[Contractor Address]

REPORT RELEASE RESTRICTIONS: See Page [number]

Page

CONTENTS: Subject of Audit
Executive Summary
Scope of Audit
Results of Audit
Contractor Organization and Systems
DCAA Personnel and Report Authorization
Audit Report Distribution and Restrictions

SUBJECT OF AUDIT

As you requested on [insert date of request], we examined [Contractor name]'s ([short name]) accounting system as of [insert date audit fieldwork was completed] to determine whether it is adequate for accumulating costs under Government contracts and whether the billing procedures are adequate for the preparation of cost reimbursement claims, i.e., interim public vouchers and progress payments.

[Short name] is responsible for establishing and maintaining an adequate accounting system for accumulating and billing costs under Government contracts. Our responsibility is to express an opinion on the adequacy of the accounting system based on our examination.

EXECUTIVE SUMMARY

If applicable (CAM 10-210.2), this section gives a brief overview of significant audit findings. Refer to 10-406 for examples. Below is an example of how the section may read when the system is inadequate in part.

The contractor's accounting system is inadequate in part. Our examination disclosed [insert number of deficiencies] significant deficiencies in [insert contractor's name] accounting system that could result in misstated costs.

SIGNIFICANT ISSUES

- [insert summary of significant issues/deficiencies]
- [if applicable][Insert contractor's name] agrees and is taking aggressive action to correct these deficiencies.

SCOPE OF AUDIT

Except for the qualifications discussed below (omit if there is no "Qualifications" section within the "Scope" paragraph), we conducted our examination in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the examination to obtain reasonable assurance about whether the data and records examined are free of material misstatement. An examination includes:

- obtaining an understanding of internal control for accumulating and billing costs under Government contracts;
- examining, on a test basis, evidence supporting the amounts and disclosures in the data and records evaluated;
- assessing the accounting principles used and significant estimates made by the contractor; and
- evaluating the overall data and records presentation.

We evaluated the accounting system using the applicable requirements contained in:

- Federal Acquisition Regulation (FAR);
- *Defense FAR Supplement (DFARS); and*
- *Cost Accounting Standards (CAS) [if applicable].*

Our examination included an evaluation to determine if the accounting system provides for the following procedures:

- *direct and indirect costs are appropriately identified, accumulated, and reported;*
- *unallowable costs are appropriately identified and segregated;*
- *indirect costs are allocated equitably and consistently to contracts and other cost objectives;*
- *direct and indirect labor costs are identified to intermediate or final cost objectives by the timekeeping system and charged to appropriate cost objectives by the labor distribution system.*
- *indirect billing rates are acceptable to the contracting officer or contract auditor in accordance with FAR 42.704;*
- *cost information for billings is based on currently posted accounting data;*
- *subcontractor and vendor costs are paid in accordance with subcontract and invoice terms and conditions and ordinarily paid prior to the contractor's next payment request to the government; and*
- *contract billings are reviewed by management to assure compliance with contract terms and provisions, e.g., frequency of billings, special withholding provisions, contract unallowables, etc.*

Our examination was performed from [fieldwork starting date] to [fieldwork completion date].

We believe that our examination provides a reasonable basis for our opinion.

Conclude the Scope section with the Inherent Limitations paragraph:

Our examination did not include tests to determine whether internal control is in operation or operating effectively. Because of inherent limitations in any internal control, misstatements due to error or fraud may occur and not be detected. Also, accounting system internal control is subject to the risk that the internal control may become inadequate because of changes in conditions.

QUALIFICATIONS

Any external factors that restrict or limit the scope of the audit should be clearly described within the scope of audit section under a separate heading entitled "Qualifications" (See 10-407e and 10-210.4). Internal decisions to limit the audit scope are not "qualifications."

When necessary to avoid user misunderstanding, scope limitations should be briefly described within the scope of audit section.

RESULTS OF AUDIT

In our opinion, *[except for the (cite the qualification and the potential impact on the results)]* *[short name's]* accounting system is *[adequate, inadequate, or inadequate in part]* for accumulating and billing costs under Government contracts.

The remaining portion of this section, excluding the last paragraph, should summarize the conditions and recommendations found during the audit. Refer to 10-408.2(b) for additional information. Below is an example of how the paragraph may read when significant deficiencies are found.

Our examination noted certain significant deficiencies in the design or operation of the accounting system. In our judgment, these deficiencies could adversely affect the organization's ability to record, process, summarize, and report costs in a manner that is consistent with applicable Government contract laws and regulations. These conditions are detailed in the "Statement of Condition(s) and Recommendation(s)" on page [xx] and summarized below:

Below is an example of how the paragraph may read when the deficiencies found are not considered significant, but correction would enhance the system.

During the course of our examination, we also noted other matters involving the accounting system which, although not considered to be significant deficiencies at this time, we believe should be communicated to the management of *[insert contractor's name]*. These matters are detailed in the "Suggestions to Improve the System" appendix included on page [xx] of this report.

Our examination was limited to determining whether *[Contractor's name]'s [short name]* accounting system is adequate for accumulating and billing costs under Government contracts. We did not perform a comprehensive examination of the contractor's overall accounting system and its related internal control. Accordingly, we express no opinion on *[short name]'s* system of internal control taken as a whole.

Conclude the Results of Audit section of the report narrative with the following additional remarks, as appropriate.

We discussed the results of our examination with *[Name and Title of contractor representative]* in an exit conference held on *[Date]*. *[If there are system deficiencies, summarize the contractor's reaction here.] [If the evaluation requires a Statement of Condition(s) and Recommendation(s) be furnished to the contractor, include the following statement].* We provided a draft copy of the *[Results of Audit and Statement of Condition(s) and*

Recommendation(s)] to the contractor's representative at the exit conference. [When the contractor provides a formal, written response, it should be referenced within the Results of Audit section and included as an appendix to the report. Put any rebuttals in the "Auditor's Response" portion of the explanatory notes and include the following statement.] The complete text of the contractor's response appears as Appendix [X].

Use the guidelines provided in 10-210.5d(2) to prepare any other additional remarks.

STATEMENT OF CONDITION(S) AND RECOMMENDATION(S)

The statements of condition(s) and recommendation(s) are an integral part of the results of audit and should follow the narrative described in the Results of Audit. Alternatively, they may be included in attached appendixes. Refer to 10-409 for detail on the presentation criteria and construction.

CONTRACTOR ORGANIZATION AND SYSTEMS

This section should furnish pertinent information necessary for the reader to understand the area audited. Refer to 10-410 for additional information. An example of wording for this section for a postaward accounting system audit follows:

1. Organization:

[Short name] was incorporated in the state of [name state] on [date]. Sales for fiscal year ended [date] were \$XX million. [Short name] has two major operations. Describe organization. [Short name's] sales are about equally divided between the two organizations.

2. Accounting System:

[Short name's] accounting period is from [date] to [date]. [Short name] maintains an accounting system on the [accrual] basis in accordance with generally accepted accounting principles. [Short name's] accounting system is posted on a current basis. Appropriate adjusting entries are made at the end of each month and at year end. [Short name] prepares financial statements on a semiannual and annual basis. The annual financial statements are not audited by external CPAs.

[Shortname] maintains a job cost accounting system which is fully integrated in the overall accounting system, wherein contracts are assigned individual project numbers and direct costs are identified and charged to those numbers. Indirect costs are identified with and accumulated under individual departments, which in turn are identified to the various indirect cost pools. Indirect expenses are recorded and billed to projects using predetermined rates. The predetermined rates are adjusted to actual rates at year end. The following schedule describes [shortname's] indirect cost pools and related allocation bases, and the type of effort normally charged direct and indirect:

Indirect Cost Pools and Allocation Bases:

<u>Indirect Cost Pool</u>	<u>Allocation Base</u>
Manufacturing Overhead	Total manufacturing direct labor dollars
Software Dev. Overhead	Total software dev. direct labor dollars
G&A Expense	Total incurred costs, excluding G&A expenses and direct subcontract costs
Fringe Benefit	Total labor dollars
Subcontract Management	Total direct subcontract costs

The Following Effort Is Normally Charged Direct:

- Direct time of direct labor employees

- *Premium (overtime, shift, field) time of direct labor*
- *Raw material, purchased parts and subcontracted items*
- *Travel expenses incurred by direct employees*
- *Freight charges for direct raw materials, purchased parts, and subcontracted items*
- *Purchase, fabrication or rental of special tooling or test equipment*
- *Professional services and consultant fees*
- *Temporary help to perform direct effort*

The Following Effort Is Normally Charged Indirect:

- *Management, supervisory, and clerical salaries*
- *Indirect time of direct employees*
- *Premium (overtime and shift) of indirect employees*
- *Social Security, unemployment insurance, workmen's compensation, group insurance, pension expense, vacation and holiday pay*
- *Guard expense*
- *Travel expense associated with indirect labor effort*
- *Other expenses such as general operating supplies, depreciation,*
- *employee wellness programs, utilities, rental costs of facilities,*
- *and general purpose equipment*

3. Billing System:

[Short name's] has about 15 employees who work in the billing department. The billing department is responsible for preparing all cost reimbursement claims, including public vouchers, progress payment requests and invoices, submitted to the government. Billings are prepared directly from the cost accounting records which are reconcilable by cost element for all cost-reimbursable work. Direct labor hours are included in the cost accounting records for labor hours, time and material and level of effort contracts. The contractor's indirect billing rates are established in accordance with FAR 42.704. The contractor participates in the DCAA direct billing program and electronically submits interim vouchers and progress payments to Defense Finance and Accounting Services paying offices via the WINs Internet payment initiate. During last Fiscal Year 20XX, [Short name] billing department submitted about \$25 million of cost reimbursement billings to the government.

Audit Report No. [XXXX-XXXXX17740XXX]

DCAA PERSONNEL

Primary contacts regarding this audit:

, Auditor

, Supervisory Auditor

Telephone No.

Other contacts regarding this audit report:

, Branch Manager

, Financial Liaison Advisor

FAX No.

, Financial Liaison Advisor

E-mail Address

General information on audit matters is available at <http://www.dcaa.mil/>.

RELEVANT DATES

Use this section in demand assignments. These should include, at a minimum, the dates of ACO and PCO requests and the dates of any extensions. The format should facilitate computation of elapsed days (see 10-211 and Fig. 10-2-3).

AUDIT REPORT AUTHORIZED BY:

[Name]

[Title]

[FAO]

AUDIT REPORT DISTRIBUTION AND RESTRICTIONS

DISTRIBUTION

Administrative Contracting Officer

E-mail Address
[E-mail address]

[Contractor name] (Copy furnished thru ACO)
[Contractor address]

RESTRICTIONS

1. Information contained in this audit report may be proprietary. It is not practical to identify during the conduct of the audit those elements of the data which are proprietary. Make proprietary determinations in the event of an external request for access. Consider the restrictions of 18 U.S.C. 1905 before releasing this information to the public.
2. Under the provisions of Title 32, Code of Federal Regulations, Part 290.7(b), DCAA will refer any Freedom of Information Act request for audit reports received to the cognizant contracting agency for determination as to releasability and a direct response to the requestor.
3. Do not use the information contained in this audit report for purposes other than action on the subject of this audit without first discussing its applicability with the auditor.

Contractor Name
City, VA

Preaward Survey of Prospective Contractor Accounting System Audit
RISK ASSESSMENT/PRELIMINARY REVIEW

Summary of Risk Assessments

1. Internal Control

If a previous accounting system audit/survey was completed, summarize any accounting system deficiencies documented in the ICQ/permanent file and the impact of these deficiencies on this audit. (This summarizes completion of preliminary audit step 1c.)

2. Materiality and Sensitivity:

Document significant materiality and sensitivity factors (such as amount and type of the proposed government contract, customer concerns) and how they affect the scope of audit. (This summarizes completion of preliminary audit step 1a.)

3. Inherent Risk Assessment:

Document significant inherent risk factors (such as size and structure of contractor, financial condition, prior audit findings, if applicable, etc.) and how they affect the scope of audit. (This summarizes completion of preliminary audit steps 1c and 3.)

4. Fraud Risk Assessment:

Document any identified fraud risk indicators and your response/actions to the identified risks (either individually or in combination). Document the effect on the scope of this audit. If no risk indicators are identified, document below. (This summarizes completion of preliminary audit step 1e.)

5. Results of Risk Assessment Procedures

Based on the risk factors identified in steps 1-4 above, document the scope of the audit including the nature and extent of testing. In determining the scope of audit, establish audit procedures to understand the design of the system to ensure the reliability of computer-based data. If reliability of the computer based data cannot be sufficiently

B

Auditor:	
Date:	

Contractor Name
City, VA

Preaward Survey of Prospective Contractor Accounting System Audit
RISK ASSESSMENT/PRELIMINARY REVIEW

determined, the audit report should be qualified in accordance with CAM 10-210.4. (This summarizes completion of preliminary audit step 3.)

REVIEWER’S APPROVAL AND DATE:

(Reviewer’s Approval)

OTHER REVIEWER AND DATE:

(If Applicable)

B

Auditor:	
Date:	

Contractor Name
City, VA

Post Contract Award Accounting System Audit at Nonmajor Contractors
 RISK ASSESSMENT/PRELIMINARY REVIEW

Summary of Risk Assessments

1. Internal Control

Summarize any outstanding accounting system deficiencies documented in the ICQ and/or permanent file and the impact of these deficiencies on the audit. Include in this documentation the results of any prior preaward and/or post contract award accounting system audits and how the results affect the scope of this audit. This summarizes completion of preliminary audit steps 2.a. & 2.d.

2. Materiality and Sensitivity:

Document significant materiality and sensitivity factors (e.g., amount and type of government contracts, customer concerns) and how they affect the scope of audit. (This summarizes completion of preliminary audit steps 1 & 2.e.)

3. Inherent Risk Assessment:

Document significant inherent risk factors (e.g., prior audit findings, audit leads, size and structure of contractor, financial condition, etc.) and how they affect the scope of audit. This summarizes completion of preliminary audit steps 2.b, 2.c, 4, 5, and 7).

4. Fraud Risk Assessment:

Document any identified fraud risk indicators and your response/actions to the identified risks (either individually or in combination). Document the effect on the scope of this audit. If no risk indicators are identified, document below. This summarizes completion of preliminary audit step 6.

5. Results of Risk Assessment Procedures:

Auditor:	
Date:	

Contractor Name
City, VA

Post Contract Award Accounting System Audit at Nonmajor Contractors
RISK ASSESSMENT/PRELIMINARY REVIEW

Based on the risk factors identified in steps 1-4 above and the audit work performed on W/P B-2 (i.e., determining the reliability of computer-based data), document the scope of the audit including the nature and extent of testing. This summarizes completion of preliminary audit steps 3 & 8.

REVIEWER'S APPROVAL AND DATE:

(Approval required prior to
performance of detailed audit steps).

OTHER REVIEWER AND DATE:

(If Applicable)

Auditor:	
Date:	

Contractor Name
City, VA

Post Contract Award Accounting System Audit at Nonmajor Contractors
RISK ASSESSMENT/PRELIMINARY REVIEW

Documentation on the Reliability of Computer-Based Data

Is the contractor's submission supported by data from computer-based systems on which you will significantly rely to reach your conclusion?

Yes ☐

No ☐

If yes, document or reference below one or more of the following: (1) where the reliability of the data was sufficiently established in other DCAA audits (e.g., floor checks or incurred cost audits) or by other non-DCAA auditors (CAM 4-1000); (2) the audit procedures being performed in this audit that will determine the reliability of the data; and/or (3) the additional testing planned for this audit that will specifically determine the reliability of the data (e.g., directly testing the data to source documents; evaluate computer reports for completeness, obvious errors and reasonableness of amounts; and confirming the computer-processed data with product users). Incorporate these procedures in the scope of audit. If reliability of the computer based data cannot be sufficiently determined by completing (1), (2), or (3) above, the audit report should be qualified in accordance with CAM 10-210.4.

DESCRIPTION OF DMIS VERSION 3.1 MODIFICATIONS

Assignment Setup

On the Setup tab, auditors will be required to identify the type of audit being performed before saving the assignment. This will be accomplished via use of a pop-up box which will be triggered by the command to save the Setup information. The auditor will have to select between two choices – “Preaward Survey” and “Post Contract Award Accounting System Audit” before being able to successfully save the Setup data and proceed. The type of audit identified in the pop-up box will be stored in the field entitled “Agency Wild Card 2, ASN_WILD_CARD_AGENCY_2_TX”. Therefore, on Code 17740 assignments, auditors should not make entries in the Agency Wild Card 2 field. DMIS will allow for searches to be performed on this field, which will group the assignments by type (Preaward Survey or Post Contract Award).

Assignment Disposition

Currently, DMIS does not allow auditors to enter the type of opinion rendered, i.e., the “Audit Opinion Code” box does not allow entries. With release of DMIS version 3.1, the “Audit Opinion Code” box will be opened, and auditors should document the type of opinion rendered. A drop-down box will be provided with the following options:

- 1 = The system is adequate.
- 5 = The system is inadequate or inadequate in part.
- 6 = Contracting officer resolution complete or follow-up report issued.
- 7 = The system is acceptable.
- 8 = The system is acceptable with the recommendation that an accounting system audit be performed after contract award
- 9 = The system is not acceptable

As explained previously, the Preaward Survey will report on the acceptability of the system design, and the Post Contract Award audit will report on the adequacy of the system. Based on the initial designation under the Setup tab of which type of audit is being performed, DMIS will automatically provide the appropriate options. In other words, if an auditor identifies that a Preaward Survey is being performed, then options 1 and 5 will not be available for selection under the “Audit Opinion Code” box. If an auditor identifies that a Post Contract Award audit is being performed, then options 7, 8, and 9 will not be available for selection under the “Audit Opinion Code” box.